

# IDAHO OUTLOOK

## NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO

DIVISION OF FINANCIAL MANAGEMENT

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Most economic forecasts focus on the short term of one to five years out. In this issue of the *Idaho Outlook* we take the longer perspective of a quarter century. To do this, we share the findings from Global Insight's most recent 25-year economic forecast. We will look at three different projections (*trend, optimal, and pessimistic*) for the U.S. economy and a *Trend Forecast* for Idaho's economy.

The factors that fuel long-run economic growth are different than those that influence short-term growth. In general, long-term growth is determined by supply factors, but short-term growth is demand driven. For example, the long-term output is determined by a combination of labor supply, capital supply, and technology. These items tend to change slowly over time, so a chart of output over a long period is relatively smooth. On the other hand, a graph of output for a short period is rough due to changes in demand for consumer goods and services, business investments, government spending, exports, and imports. Fiscal and monetary policies have both short and long-term impacts. For example, well-timed federal spending could stimulate the economy and shorten a recession. A permanent tax cut could fuel investment in capital goods, which would increase long-term growth.

In the *U.S. Trend Forecast*, real GDP growth averages 3.1% per year from 2003 to 2029, which is slightly above its estimated potential of 2.9%. This growth reflects the anticipated 0.9% average growth of the U.S. labor force and anticipates 2.4%

annual increases in productivity. The favorable productivity growth keeps inflation near 2.0% through the forecast period. The economy grows slightly faster over the next 25 than during the most recent quarter century (1978-2003). Interestingly, real output grew slightly slower than its potential over the last 25 years. Another difference between the next quarter century and the most recent one is the role of the consumer. Real consumer spending grew faster than real output from 1978 to 2003, but will advance slightly slower than output from 2003 to 2029. Part of this gap will be taken up by stronger business investment, which is projected to increase 6.4% annually compared to the historical rate of 3.8%. Exports are also expected to grow faster (7.1%) in the future than in the recent past (5.2%). The outlook for the government sector has been scaled back the most; it is projected to expand just 1.5% per year, compared to its historical average of 2.3%.

We now turn to the *U.S. Optimistic Forecast* that explores how just changing a few assumptions would affect the long-term economic outcome. Space limitations dictate that we focus on labor force and productivity growth, but readers are reminded these are not the only factors influencing the future direction of the economy. In Global Insight's *U.S. Optimistic Forecast* the labor force advances 1.1% per year and productivity rises 2.7% annually. These changes help boost the expected trajectory of the U.S. economy. Potential output speeds up by one-half percentage point compared to the trend output, 3.4% versus 2.9%. Real GDP rises 3.6%

annually, compared to the trend's 3.1%. Despite the significantly stronger growth, inflation is actually lower in the optimistic forecast than in the trend forecast.

In the *U.S. Pessimistic Forecast*, both the labor force and productivity fall below their trend forecast's paces. The labor force is 0.8% per year, slightly below the 0.9% growth assumed in the trend forecast. On the other hand, the difference between the trend and pessimistic forecasts is huge, 1.9% versus 2.4%. This difference contributes to both the lower potential GDP and actual GDP. Specifically, potential GDP growth has been reduced to 2.3 % per year and real output is forecast to expand just 2.6% annually. Both of these measures are not only lower than their trend counterparts, but are lower than their historical levels. Despite the anticipated slower growth, inflation averages about 3.2% per year, which is higher than both its trend and optimistic levels.

In the *Idaho Trend Economic Forecast*, the state out performs its national counterpart over the next quarter century. For example, Idaho nonfarm employment should advance just over 2% per year from 2004 to 2029. In comparison, U.S. nonfarm employment is expected to increase 1.2% annually. Idaho real disposable personal income grows slightly faster than its national counterpart. However, Idaho real per capita disposable income grows slower than at the national level, a consequence of the state's relatively fast growing population.

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## General Fund Update

As of October 31, 2004

<u>Revenue Source</u>	<u>\$ Millions</u>		
	FY05 Executive Estimate <sup>3</sup>	DFM Predicted to Date	Actual Accrued to Date
Individual Income tax	968.0	281.9	293.6
Corporate Income tax	118.9	33.1	35.3
Sales Tax	910.8	318.3	332.4
Product Taxes <sup>1</sup>	21.9	7.7	8.1
Miscellaneous	105.7	30.1	31.0
<b>TOTAL GENERAL FUND<sup>2</sup></b>	<b>2,125.3</b>	<b>671.0</b>	<b>700.4</b>

<sup>1</sup> Product Taxes include beer, wine, liquor, tobacco and cigarette taxes  
<sup>2</sup> May not total due to rounding  
<sup>3</sup> Revised Estimate as of August 2004

General Fund revenue exceeded expectations for the fourth straight month in October, coming in \$4.2 million higher than expected. This is the mildest performance so far this fiscal year, but it brings the fiscal year-to-date excess to \$29.4 million. October's excess was overwhelmingly due to strong individual income tax collections, partially offset by weakness in the corporate income tax. All revenue categories are ahead of expectations on a year-to-date basis, with the individual income tax and the sales tax leading the pack.

Individual income tax collections were \$6.5 million higher than expected in October, more than doubling the year-to-date excess.

For the month, both filing and withholding collections exceeded expectations, and were partially offset by higher-than-expected refunds. On a cumulative basis all three major components of the individual income tax (filing collections, withholding collections, and refunds) are performing better than expected.

Corporate income tax collections were \$3.6 million lower than expected in October, but are still \$2.2 million ahead of fiscal year-to-date expectations. October's weakness was concentrated on the refund side, with refunds running \$3.0 million higher than expected. Refunds are \$2.1 million higher than expected on a year-to-date basis. Quarterly estimated payments

are \$0.4 million lower than expected for the first four months of the fiscal year, but filing payments are \$4.7 million higher than expected for the same period.

Sales tax collections were very close to the target for October, coming in just \$0.5 million higher than expected. This brings the sales tax to \$14.1 million ahead of the fiscal year-to-date target. This is the second month of cooling from the red-hot pace of July and August.

Product taxes were again \$0.1 million above target in October on strong cigarette tax collections. Miscellaneous revenue was \$0.6 million higher than expected in October as a consequence of strength in interest earnings and miscellaneous transfers.